

Executive Summary

This report provides a review and evaluation of Kentucky's economy as well as the General Fund and Road Fund for the second quarter of Fiscal Year 2005 (FY05). General Fund receipts totaled \$1,962.2 million in the second quarter, an increase of 7.5 percent from the second quarter of FY04. This represents \$137.5 million more than reported in the same period of FY04.

Road Fund receipts in the second quarter of FY05 were \$256.7 million, a decline of 0.7 percent from the second quarter of FY04. This is \$1.6 million less than reported in the same period of FY04.

The second quarter of FY05 saw the national economy continue to register solid gains. Real gross domestic product (GDP) expanded at an annual rate of 3.6 percent in the second quarter. Personal income, a measure of spending power, likewise rose by a sharp 9.5 percent. Nonagricultural employment growth has begun to accelerate in recent months, rising 1.8 percent on an annualized basis. Manufacturing employment, which had been shrinking, continued this trend by falling 0.2 percent in the second quarter.

Kentucky's personal income was estimated at \$116.7 billion in the second quarter of FY05, representing an increase of 5.4 percent from one year ago. Nonagricultural employment in the Commonwealth rose by 1.2 percent when compared to the previous year, with a gain of 21,700 jobs. Construction, trade, transportation and utilities, finance, business services, and government all reported healthy gains in employment. Declining sectors included mining, information services, and "other" services.

General Fund receipts in the second quarter were boosted by gains in several of the largest revenue sources. Performance by major tax or revenue category is summarized in Table 3 on page 9. Among the major accounts, the sales and use tax grew by 3.6 percent compared to the second quarter of FY04. The individual income tax rose by 5.6 percent, and the combined corporation income and license taxes grew by 35.6 percent. The coal severance tax has recently been rising sharply, and this trend continued in the second quarter with receipts up by 24.6 percent. Property taxes were up 12.7 percent due to timing differences, and the lottery grew by 4.4 percent. All other taxes in the General Fund combined for a growth of 5.3 percent.



The Road Fund posted a decline in the second quarter of FY05, falling 0.7 percent with total revenues of \$256.7 million. Summary data on second-quarter Road Fund receipts appears in

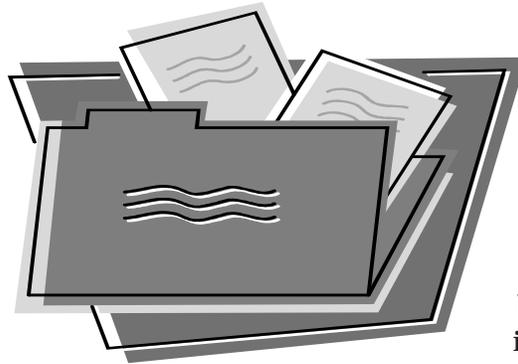
Table 4 on page 10. During the second quarter, motor fuels taxes rose by 3.6 percent, primarily as a consequence of the formula-driven increase in the motor fuels tax rate. The motor vehicle usage tax declined by 5.8 percent, and the weight distance tax grew by 6.1 percent. The 3.4 percent decline in the "all other" category was principally due to decreases in highway tolls and investment income.

The national economic outlook for the next two fiscal quarters of FY05 is for GDP growth to average 3.7 percent. In Kentucky, personal income should grow by 4.5 percent in the

January-June 2005 period, compared to 4.9 percent nationally. For the first quarter of FY06, GDP is expected to rise by 3.6 percent, and Kentucky personal income should also rise by 4.9 percent.

The interim outlook for the General Fund is for revenues to grow by 5.2 percent in the final two quarters of FY05. This forecast for the General Fund is presented in Table 6 on page 16. This interim estimate is identical to the official estimate for FY05. The improving economy is expected to allow growth to continue, but not at the rate achieved during the first two quarters.

Sales tax revenues should rise 5.6 percent in the final two quarters of FY05, and individual income taxes are expected to grow 5.3 percent. Corporation income and license taxes are forecasted to rise sharply, while property taxes will decline by 6.8 percent. The lottery should rise by 2.5 percent despite increased competition from the Tennessee lottery, but "other" taxes and revenues will decline primarily due to lower inheritance tax and abandoned property revenues.



The interim General Fund forecast for the first quarter of FY06 anticipates a growth rate of 2.6 percent over the prior year. Principal drivers of the growth include the individual income tax, the sales and use tax, and property taxes.

The interim forecast for the Road Fund is for an increase of 2.2 percent in the final two quarters of the fiscal year. This interim estimate is identical to the official estimate for FY05. The interim forecast for the Road Fund is summarized on attached Table 7 on page 17.

Motor fuels taxes are expected to grow by 8.1 percent in the second half of FY05, mainly due to a continuation on the one-cent rate increase tied to the wholesale price of motor fuels. Motor vehicle usage tax revenues should fall by 4.2 percent in the remaining two quarters of the fiscal year, and weight distance taxes should expand by 4.0 percent. License and privilege taxes (excluding the weight distance tax) are expected to fall by 0.2 percent. Toll revenue is forecasted to decline by 7.5 percent, but investment income should be up 113.3 percent on a very small base. All other revenue sources in the Road Fund are forecasted to fall by 0.9 percent in the final half of the fiscal year. For the first quarter of FY06, the Road Fund is projected to rise by 1.9 percent over the first quarter of FY05.

The Economy

NATIONAL ECONOMY

Second Quarter, FY05

Real gross domestic product (GDP) is an inflation-adjusted measure of the total output of goods and services produced in the United States. Real GDP is estimated to have increased by a robust 3.6 percent in the second quarter. During the previous quarter the growth rate was 4.0. This marks the return of a much-awaited growth pattern in which output grows between 3.5 percent and 4.5 percent. Growth rates within this range are thought to be optimum for increasing employment.

The strength of the domestic economy continues to be derived from the consumer.

Consumption expenditures account for about two-thirds of real GDP. Real consumption was up 3.8 percent in the second quarter following a

remarkable increase of 5.1 percent in the first quarter. There was a marked slowdown in the consumption of durable goods, up just 1.7 percent, compared to a 17.2 percent increase in the previous quarter. The deceleration resulted from a decline in motor vehicles and parts. The sharp gain in gasoline prices and the lack of automobile incentives during the October-to-December quarter caused auto consumption to contract by 1.7 percent compared to a 28.7 percent increase in the previous quarter. This wasn't altogether

surprising as consumers took a respite from the auto market and focused their spending on Christmas presents. Consumption of nondurable goods was up 5.0 percent. Nondurables are normally quite stable and not prone to swings from interest rates and incentives. However, in this quarter there were some swings within this category and consumption patterns moved in favor of gasoline and food. Services constitute a little over one-half of all consumption and about 35 percent of total GDP. The consumption of services increased by 3.7 percent in the second quarter. Much of the increase came from the area of personal and business services which were up 6.6 percent.

Investment spending proved to be the light at the end of the recession tunnel. Total investment comprises close to a fifth of real GDP and is usually sensitive to both interest rates and future expansion opportunities. The investment component of GDP increased by 8.0

percent during the second quarter after posting 2.4 percent growth in the previous quarter. Equipment and software continued to be a strong driver in this category with a growth of 10.2 percent.

The Governor's Office for Economic Analysis monitors industrial production because it is a measure of the output of heavy industries like mining and manufacturing. These industries continue to play a vital role in Kentucky's economy. Industrial production is a raw measure of output, comprised of only the final



products. Total industrial production was up 3.8 percent during the second quarter and 2.9 percent in the first quarter. Just a year ago industrial production was declining in response to factors like the lack of consumer confidence and the consequent drop in demand. Other factors that depressed industrial production were overcapacity in production facilities abroad and the strong dollar. Both these fueled imports at the expense of domestic production. Now, however, with the economic recovery well underway and the U.S. dollar at a historic low with respect to both the euro and yen, industrial production is on the rise.

Personal income, which is a measure of spending power, was \$9,896.1 billion in the second quarter, for an annualized increase of 9.5 percent over the previous quarter. Real disposable income was up 7.4 percent, and real expenditure was up 3.8 percent. The extraordinary gain in personal income resulted from a surge in dividends, interest, and rent. This category is about one-sixth of total personal income and posted gains of 37.7 percent in the second quarter.

Inflation was up by 3.5 percent as energy prices soared. Even excluding the relatively volatile food and energy sector, inflation was up 2.4 percent. The unemployment rate stayed steady at 5.4 percent, the same as the previous quarter. Nonfarm employment posted a strong gain of 1.8 percent during the second quarter. Both construction and mining had large increases, though manufacturing declined.

STATE ECONOMY

Kentucky was affected by the relatively languid growth in employment as productivity pushed output to the detriment of jobs. Current data indicates that although employment has not returned to March 2000 levels, there has been positive movement in

the economy in response to the federal fiscal and monetary stimulus. Key measures like employment and income firmed up during the second quarter indicating that Kentucky is on a steady path to recovery.

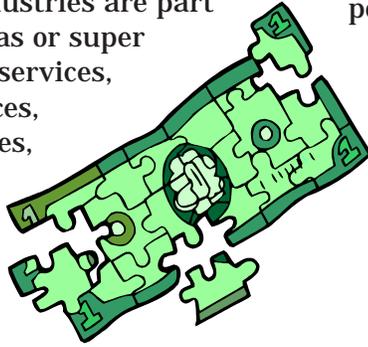
Kentucky's personal income is estimated to be \$116.7 billion in the second quarter of FY05, an increase of 5.4 percent from a year ago. U.S. personal income grew by 6.1 percent during the same period. Wages and salaries constitute a little over half of personal income. Income derived from wages and salaries is estimated to have grown by 4.2 percent in FY05:2.

Employment data is commonly used to gauge the strength of the state's economy, primarily because of its timely availability and its impact on consumer spending and confidence. Kentucky gained approximately 21,700 jobs during the second quarter compared to a year ago. This is a decided gain for the state economy, especially coming in wake of a loss of nearly 3,600 jobs during the same period a year earlier.

Manufacturing jobs in Kentucky have been the hardest hit by the recession. During the second quarter manufacturing employment steadied to the extent that there was no net job loss. At the moment the only positive statement that can be made about manufacturing is that zero growth is definitely better than the 5.3 percent contraction that occurred during the second quarter of FY04. Nationally, manufacturing employment is estimated to have increased by 0.4 percent during the October-to-December 2004 period. The national gains were primarily from the durable-goods sector, especially in the area of wood products and transportation equipment. Among the large industries hardest hit in Kentucky were electronic and electrical equipment, and fabricated metal productions. Both these sectors have suffered nationally as jobs have moved overseas. In contrast, Kentucky's

automotive sector posted a strong gain of 1.2 percent.

A little over one-third of Kentucky's nonagricultural jobs are in the services sector. The broad service-related industries are part of four newly categorized areas or super sectors. These are: business services, educational and health services, leisure and hospitality services,



and other services. Overall employment in services was up 1.0 percent with the strongest gains in business services (up 4.3 percent). The business service category is dominated by temporary employment services, and it is possible that the strong growth in this sector is from the reluctance of businesses to hire permanent employees until the economic recovery has firmed-up.

Table1
National Economic Indicators
Second Quarter, FY05

	FY04:2	FY05:1	FY05:2	SAAR** FY05:1 to FY05:2	FY04:2 to FY05:2 Percent Change
Real GDP (billion 2000 \$)	10,581.0	10,891.0	10,988.0	3.6	3.8
Personal Income (billion \$)	9,330.0	9,674.3	9,896.1	9.5	6.1
Real Disposable Income (billion 2000 \$)	7,849.6	7,990.2	8,134.4	7.4	3.6
Consumer Price Index (annual percent change)	0.7	1.9	3.5	-	-
Industrial Production (annual percent change)	5.7	2.9	3.8	-	-
Civilian Labor Force (millions)	147.0	147.7	148.2	1.5	0.8
Total Nonagricultural Employment (millions)	130.0	131.5	132.1	1.8	1.6
Manufacturing Employment (millions)	14.3	14.4	14.4	-0.2	0.4
Unemployment Rate (percent)	5.9	5.4	5.4	-	-

Sources: Global Insight, Inc., and U.S. Dept. of Commerce, Bureau of Economic Analysis.

* Data for FY05:2 are January 2005 estimates.

** Seasonally adjusted annual percent growth rate.

Table 2
Selected Kentucky Economic Indicators
Seasonally Adjusted Data

	FY04:2	FY05:2	Percent* Change
Total Personal Income (\$ millions)	110,691	116,691	5.4%
Wage & Salary Income (\$ millions)	59,965	62,485	4.2%
Total Nonagricultural Employment	1,786.0	1,807.7	1.2%
Contract Construction	84.7	88.0	4.0%
Mining	19.1	18.9	-1.0%
Manufacturing	266.0	266.0	0.0%
Trade, Transportation & Utilities	371.8	378.1	1.7%
Information	30.1	29.9	-0.6%
Finance	86.2	87.6	1.7%
Business Services	154.7	161.3	4.3%
Educational and Health Services	229.6	232.2	1.1%
Leisure and Hospitality Services	158.7	159.2	0.3%
Other Services	78.2	74.5	-4.7%
Government	306.9	312.0	1.7%

* Seasonally adjusted rate from a year ago.

Source: GOEA, January 2005.

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Revenue Receipts

Second Quarter FY2005

General Fund

The second quarter of FY05 experienced continued robust growth following a strong first quarter of this fiscal year. FY05 growth rates were boosted by increased receipts from the corporation income and license taxes, the coal severance tax, and a one-time sale of securities earmarked for a prepaid tuition program. Receipts in the second quarter totaled \$1,962.2 million compared to \$1,824.7 million received in the second quarter of FY04.

The resulting growth rate was 7.5 percent, and compares to a growth rate of 1.3 percent for the same quarter last year. Collections in the major revenue categories are shown in summary form in Table 3. Detailed information on these and other accounts is available in the Appendix.

Variations in the quarterly receipts are often affected by differences in the timing of payments into revenue accounts. While timing differences were not as prevalent as in the past, property tax receipts continue to record fluctuations because of these differences.

Total sales and use tax receipts for the quarter were \$642.8 million, compared to \$620.3 million in the second quarter of

FY04. The result is a growth rate of 3.6 percent and matches the growth rate for the second quarter of last year.

Individual income tax posted receipts of \$739.1 million, compared to last year's second-quarter receipts of \$699.7 million. The resulting growth rate was 5.6 percent, and compares to a growth rate of 2.5 percent for the second quarter of last year.

Combined corporation income and license tax receipts grew strongly in the second quarter of the fiscal year. Revenues of \$114.7 million were 35.6 percent higher than year-earlier figures of

\$84.6 million. Strong declaration payments and fewer refunds accounted for the growth in this account.

Second-quarter property tax receipts posted revenues that were 12.7 percent higher than the second quarter of FY04. FY05 second-quarter receipts of \$253.0 million compare with \$224.4 million from the second quarter of FY04.

Coal severance tax revenue continued to grow in the second quarter, with receipts up by 24.6 percent. Collections of \$44.1 million compare to the FY04 second-quarter total of \$35.4 million.

Lottery receipts were \$41.8 million which were \$1.8 million or 4.4 percent more than last year's second-quarter total.

Type Tax	FY05	FY04	Percent Change
Sales and Use	642.8	620.3	3.6
Individual Income	739.1	699.7	5.6
Corporation Inc./Lic.	114.7	84.6	35.6
Coal Severance	44.1	35.4	24.6
Property	253.0	224.4	12.7
Lottery	41.8	40.0	4.4
All Other	<u>126.7</u>	<u>120.3</u>	<u>5.3</u>
TOTAL	1,962.2	1,824.7	7.5

The “all other” category, which represents the remaining accounts of the General Fund, showed steady growth, posting a 5.3 percent increase in the second quarter. Second-quarter receipts for FY05 were \$126.7 million and compare to \$120.3 million in FY04.

Road Fund

The Road Fund reported a decrease of 0.7 percent in the second quarter of FY05. Receipts totaled \$256.7 million and compare to \$258.3 million from the second quarter of last year. Summary data are contained in Table 4 and detailed data are shown in the Appendix.

Motor fuels tax receipts grew at a rate of 3.6 percent during the second quarter due to the formula-driven increase in the tax rate tied to the price of gasoline. Receipts were \$112.6 million and compare to \$108.7 million collected during the second quarter of last year.

Motor vehicle usage tax declined in the second quarter, with receipts down by 5.8 percent. Receipts during the second quarter of FY05 totaled \$92.3 million and compare to \$97.9 million collected during the same period last year.

Weight distance tax receipts of \$20.8 million represent a 6.1 percent increase over receipts of \$19.6 million during the second quarter of FY04.

The remainder of the accounts in the Road Fund combined for a decrease of 3.4 percent from a year earlier. In the “all other” category, revenues of \$31.0 million compare to \$32.1 million in the second quarter of FY04.

**Table 4
Summary Road Fund Receipts
Second Quarter, FY 2005
(millions of dollars)**

<u>Type Tax</u>	<u>FY05</u>	<u>FY04</u>	<u>Percent Change</u>
Motor Fuels	112.6	108.7	3.6
Motor Vehicle Usage	92.3	97.9	-5.8
Weight Distance	20.8	19.6	6.1
All Other	<u>31.0</u>	<u>32.1</u>	<u>-3.4</u>
TOTAL	256.7	258.3	-0.7

Economic and Revenue Outlook

Final Two Quarters of FY2005 & First Quarter of FY2006

ECONOMIC OUTLOOK: Interim Forecast

The economic outlook presented here is for the three-quarter period from January to September 2005. In terms of fiscal years this period is the second half of FY05 (quarters 3 and 4) and the first quarter of FY06. The national outlook is based on Global Insight's January 2005 forecast, and the Kentucky outlook is from GOEA's January 2005 forecast. The economic outlook is identical to the one the Consensus Forecasting Group used earlier in the month in its deliberations.

National Economy

During FY05 all indicators associated with a broad recovery are strongly positive. Real GDP has been moving strongly for the past seven quarters and was up 3.9 percent in the first half of FY05 compared to the same period in FY04. Other factors like investment, productivity, and consumer confidence show robust growth. And finally, even employment has shown a slight upward movement during the first two quarters of FY05.

During the second half of FY05 real GDP is expected to grow by 3.7 percent from a year ago. Growth is expected to moderate to 3.6 percent in the first quarter of FY06 primarily because the corresponding quarter in FY05 had shown robust growth at 5.0 percent. Employment in nonagricultural industries, which had shown little growth during the recovery so far, is forecasted to post robust job

gains at 1.7 percent during the remainder of the fiscal year, and then by 1.9 percent in FY06:Q1.

The consumption component of GDP has recently been the major factor in sustaining growth. During the last two quarters of FY05 real consumption expenditures are projected to increase by 3.5 percent with durable goods rising dramatically by 5.3 percent. Consumption growth during the FY06:Q1 is expected to be 3.0 percent. The slight drop is from the expected decline in motor vehicle sales.

Investment spending has been accelerating in recent months, and the outlook is for a continuation of that trend. During the second half of FY05 investment is expected to rise by 6.7 percent, and then by 5.6 percent in the first quarter of FY06. The surge in investment is from the expectation that consumer demand will increase and the economy will continue to expand.

The weak dollar is expected to cause a surge in exports, but at the same time it is not weak enough to squelch the appetite for relatively cheap foreign goods. U.S. exports are forecasted to show gains of 8.4 percent in the latter half of FY05 and 10.6 percent in the first quarter of FY06. The corresponding import numbers are 7.1 percent and 6.5 percent.

State Economy

The impact of the national recovery is being felt in the state economy. However, the dominance of the goods-producing sector in



the state economy has slowed the recovery. During the final two quarters of FY05 personal income is estimated to increase by 4.5 compared to a 5.3 percent increase nationally. The recovery is expected to be stronger during the first quarter of FY06 with income growth of 4.9 percent compared to the national average of 5.8 percent. The relative strength in the national income figures is primarily from the robust performance of income derived from dividends, interest, and rent.

During the first half of FY05 total nonagricultural employment in Kentucky was up just 0.5 percent compared to a year ago. A combination of factors are, however, expected to push employment growth to 1.5 percent in the second half of the year, followed by a robust 1.8 percent growth in the first quarter of FY06. These factors are related not to just a boost in consumer confidence and the subsequent increase in consumer demand, but also to increased investment and exports.

Employment in goods-producing industries had declined dramatically in Kentucky in response to productivity gains and the shift of some manufacturing facilities abroad. However, the lower dollar and increased consumer demand are expected to result in gains in manufacturing jobs by the first quarter of FY06. During the second half of FY05 employment in the goods-producing sector is expected to be up by a slim 0.7 percent. During the first quarter of FY06, however, as manufacturing recovers employment in the goods-producing sector is expected to be up 2.4 percent.

Service-providing industries are forecasted to do well during the second half of FY05 with an addition of 18,300 jobs. The growth rate during the first quarter of FY06 is expected to be a robust 2.1 percent. The improvement in employment is related to the continuing expansion of business services and health care services which have done well in Kentucky even during the recession years.

Table 5
Economic Outlook: Second Half of FY05 and the First Quarter of FY06

	<u>FY04</u> <u>Q3 & Q4</u>	<u>FY05</u> <u>Q3 & Q4</u>	<u>Percent</u> <u>Change</u>	<u>FY05</u> <u>Q1</u>	<u>FY06</u> <u>Q1</u>	<u>Percent</u> <u>Change</u>
United States						
Real GDP (bil96\$)	10,741.1	11,134.7	3.7%	10,891.0	11,280.4	3.6%
Personal Income (bil\$)	9,518.9	10,019.9	5.3%	9,674.3	10,231.3	5.8%
Nonagricultural Employment (mil)	130.7	133.0	1.7%	131.5	134.0	1.9%
Unemployment Rate (%)	5.6	5.3	-	5.4	5.2	-
Kentucky						
Personal Income (mil\$)	112,711	117,792	4.5%	114,601	120,181	4.9%
Wage & Salary Income (mil\$)	60,912	63,612	4.4%	62,057	64,972	4.7%
Nonagricultural Employment ('000)	1,789.7	1,816.8	1.5%	1,799.2	1,830.8	1.8%
Goods producing ('000)	370.8	373.5	0.7%	369.4	378.2	2.4%
Service Providing ('000)	1,112.6	1,130.9	1.6%	1,117.1	1,140.1	2.1%

GENERAL FUND

Projected General Fund revenues for the next three quarters are shown in Table 6 on page 16. General Fund revenues were \$3,723.6 million in the first two quarters of FY05, a growth rate of 7.8 percent from the same period a year ago. Revenues grew strongly primarily due to improved economic performance as most major categories of revenues saw gains. However, first-half growth was strongest in the volatile corporation income and license taxes as well as coal severance taxes, all of which are expected to moderate in the remainder of FY05.

Anticipated revenues for the last two quarters of FY05 are \$3,709.4 million, corresponding to a growth rate of 5.2 percent from the previous fiscal year. Growth is expected to be positive in all major accounts except for the property tax. This forecast is identical to the official forecast prepared by the Consensus Forecasting Group on January 19, 2005.

Total sales and use tax receipts for the first half of FY05 were \$1,287.2 million, representing an increase of 5.0 percent from the same period one year ago. The projected rate of growth for the remaining two quarters of FY05 is 5.6 percent. Total sales and use tax receipts for FY05 are estimated to be \$2,577.4 million.

The interim forecast for the individual income tax calls for a growth of 5.3 percent for the remainder of FY05, amounting to collections of \$1,466.9 million in the final six months. The individual income tax rose by 5.5 percent in the first half of FY05. For the entire fiscal year, individual income tax receipts are projected to grow by 5.4 percent.

The outlook for corporation income and license taxes projects an increase of 28.5 percent in the final two quarters of FY05, representing collections of \$325.8 million.

These anticipated collections will bring the FY05 total to \$572.0 million, an increase of 33.8 percent from FY04. Revenues in FY05 for the corporate license tax will be boosted by an expected \$24.4 million when the provisions of HB 390 expire.

The coal severance tax recently reversed its long-term trend of decline and has risen for the past twelve months. The forecast is for the increases to persist for the remainder of FY05, and growth is forecasted to be robust at 9.6 percent for the remaining two quarters. Overall for the fiscal year, coal severance tax receipts are expected to rise by 16.9 percent.

Property tax revenues totaled \$291.6 million in the first six months of FY05, representing an increase of 9.8 percent. It is expected that the remaining two quarters of FY05 will yield total property tax revenues of \$170.8 million, for a drop of 6.8 percent from the previous year. Project declines are the result of timing differences, and growth for the entire fiscal year should average 3.0 percent.

Lottery revenues grew by 4.8 percent in the first half of FY05 as the state benefited from extra dividends earned due to large Powerball sales. In the next two quarters, lottery revenues are expected to continue to rise by 2.5 percent. For the entire fiscal year, lottery receipts should rise by 3.6 percent.

The “other” category contains estimates for several of the smaller revenue sources not otherwise classified. The final two quarters of FY05 should experience a sharp decline in this category due primarily to expected decreases in inheritance tax revenue and legislated changes adopted by the 2003 General Assembly that affected abandoned property receipts. For the remainder of the fiscal year, the combined “other” accounts are expected to fall by 9.0 percent.

In the first quarter of FY06, General Fund revenues are expected to rise by a moderate 2.6 percent. Sales and use taxes should grow by 4.9 percent, while the individual income tax is projected to increase by 5.1 percent. A forecasted drop in corporate income and license tax receipts is based on expectations of higher refund payments. Timing changes will affect the outlook for property taxes, lottery revenues, and "other" receipts.

ROAD FUND

Road Fund revenues over the remainder of FY05 are forecasted to grow by 2.2 percent as shown in Table 7 on page 17. This estimate is identical to the official revenue forecast adopted by the Consensus Forecasting Group on January 19, 2005.

Motor fuels tax receipts are forecasted to grow by 8.1 percent in the last two quarters of FY05. This is principally due to a change in gasoline prices and its effect on the statutory rate of the motor fuels tax.

Motor vehicle usage tax collections are expected to fall by 4.2 percent in the final two quarters of FY05. The decrease is due primarily to an administrative decision to grant a credit against the tax for Kentucky

residents who purchase their vehicle in Indiana. (Indiana recently began collecting a sales tax on motor vehicles purchased within that state by Kentucky residents. Previously, Indiana provided a credit for cars that would not be registered in that state.) In addition, lower receipts from the U-Drive-It tax on leased vehicles are also partly responsible.

To estimate the growth of all other components of the Road Fund, officials of the Kentucky Transportation Cabinet and staff of the Governor's Office for Economic Analysis together assessed recent growth patterns as well as administrative factors. License and privilege taxes are expected to decline by 0.2 percent, and toll income likewise is estimated to continue declining. Weight distance tax revenue should improve by 4.0 percent for the remainder of FY05 due to an improving economy. Investment income is forecasted to rise by 113.3 percent from a very low base. The combined "other" accounts in the Road Fund are projected to fall by 0.9 percent in the final two quarters of FY05.

In the first quarter of FY06, the Road Fund is projected to increase by 1.9 percent from the same period a year earlier. Improvements across the board, particularly in the motor vehicle usage tax, will account for much of the increase.

General Fund Interim Forecast
 (millions of dollars)
 January 2005
 Table 6

	FY05		FY05		FY05		FY06	
	Quarters 1 & 2		Quarters 3 & 4		Full Year		Quarter 1	
	Actual	% Chg Year Ago	Estimate	% Chg Year Ago	Interim* Estimate	% Chg Year Ago	Interim Estimate	% Chg Year Ago
Sales & Use	1,287.2	5.0	1,290.2	5.6	2,577.4	5.3	675.9	4.9
Individual Income	1,480.7	5.5	1,466.5	5.3	2,947.2	5.4	779.2	5.1
Corporation Income & Lic.	246.2	41.5	325.8	28.5	572.0	33.8	117.0	-11.0
Coal Severance	87.0	25.0	85.4	9.6	172.4	16.9	43.6	1.7
Property	291.6	9.8	170.8	-6.8	462.4	3.0	41.3	7.2
Lottery	86.8	4.8	93.2	2.5	180.0	3.6	41.8	-7.2
Other	244.1	5.5	277.5	-9.0	521.6	-2.7	107.7	-8.3
General Fund	3,723.6	7.8	3,709.4	5.2	7,433.0	6.5	1,806.5	2.6

* The Interim estimate for FY05 is identical to the Consensus Forecasting Group estimate finalized on January 19, 2005.

Road Fund Interim Forecast
 (millions of dollars)
 January 2005
 Table 7

	FY05		FY05		FY05		FY06	
	Quarters 1 & 2		Quarters 3 & 4		Full Year		First Quarter	
	Actual	% Chg Year Ago	Interim Estimate	% Chg Year Ago	Interim Estimate	% Chg Year Ago	Interim Estimate	% Chg Year Ago
Motor Fuels & MF Use/Surtax	243.3	5.4	247.5	8.1	490.8	6.7	129.9	2.3
Motor Vehicle Usage & Rental	201.8	-6.8	203.7	-4.2	405.5	-5.5	110.9	1.3
License & Privilege (excl. WD)	41.1	-9.0	68.0	-0.2	109.1	-3.7	21.6	2.9
Weight Distance Tax/Surtax	41.6	5.9	41.9	4.0	83.5	4.9	21.2	2.0
Toll Income	3.1	-34.8	3.0	-7.5	6.1	-23.8	1.6	0.0
Investment	1.7	-71.7	3.2	113.3	4.9	-34.7	1.0	11.2
Other	9.9	8.7	9.9	-0.9	19.8	3.7	5.2	2.0
Road Fund	542.6	-1.7	577.1	2.2	1,119.7	0.3	291.4	1.9

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APPENDIX
Second Quarter Receipts

KENTUCKY STATE GOVERNMENT REVENUE - GENERAL FUND REVENUE

	Second Quarter 2004 - 2005	Second Quarter 2003 - 2004	% Change	Year-To_Date 2004 - 2005	Year-To_Date 2003 - 2004	% Change
TOTAL GENERAL FUND	\$1,962,218,917	\$1,824,676,249	7.5%	\$3,723,601,370	\$3,452,905,759	7.8%
Tax Receipts	\$1,861,262,978	\$1,737,578,017	7.1	\$3,548,740,778	\$3,297,045,119	7.6
Sales and Gross Receipts	\$678,980,630	\$656,430,520	3.4	\$1,373,754,417	\$1,309,513,530	4.9
Beer Consumption	1,455,112	1,420,429	2.4	3,289,881	3,132,643	5.0
Beer Wholesale	9,045,064	8,515,185	6.2	19,574,916	18,905,033	3.5
Cigarette	3,915,926	4,177,808	-6.3	7,914,017	8,227,463	-3.8
Distilled Spirits Case Sales	23,103	21,904	5.5	45,362	43,585	4.1
Distilled Spirits Consumption	2,166,104	2,245,393	-3.5	4,456,738	4,465,676	-0.2
Distilled Spirits Wholesale	4,555,547	4,265,040	6.8	8,787,233	8,324,867	5.6
Insurance Premium	10,785,462	12,265,054	-12.1	35,929,070	34,762,400	3.4
Pari-Mutuel	1,384,142	750,121	84.5	1,402,860	750,109	87.0
Race Track Admission	55,418	58,931	-6.0	154,401	188,841	-18.2
Sales and Use	642,791,567	620,269,287	3.6	1,287,202,262	1,226,196,446	5.0
Wine Wholesale	2,059,924	1,925,476	7.0	3,773,734	3,534,153	6.8
License and Privilege	\$73,250,053	\$59,422,242	23.3%	\$139,643,507	\$113,664,779	22.9%
Alc. Bev. License Suspension	41,600	41,200	1.0	103,850	122,450	-15.2
Coal Severance	44,115,301	35,408,561	24.6	87,008,973	69,581,015	25.0
Corporation License	18,476,265	13,212,753	39.8	31,967,320	23,581,697	35.6
Corporation Organization	38,001	58,213	-34.7	58,344	77,173	-24.4
Occupational Licenses	24,307	14,676	65.6	81,288	54,150	50.1
Oil Production	1,223,151	755,416	61.9	2,241,855	1,571,230	42.7
Race Track License	103,750	118,925	-12.8	263,250	284,125	-7.3
Bank Franchise Tax	(202,048)	(1,853)	—	7,241	(454,538)	—
Driver License Fees	129,249	122,441	5.6	271,791	256,583	5.9
Minerals Severance	3,926,332	4,413,171	-11.0	7,626,179	8,242,744	-7.5
Natural Gas Severance	5,374,145	5,278,739	1.8	10,013,417	10,348,150	-3.2
Income	\$835,353,064	\$771,085,907	8.3%	\$1,694,980,980	\$1,553,883,369	9.1%
Corporation	96,255,629	71,354,496	34.9	214,272,655	150,405,835	42.5
Individual	739,097,435	699,731,411	5.6	1,480,708,325	1,403,477,534	5.5
Property	\$253,029,671	\$224,439,004	12.7%	\$291,591,783	\$265,451,957	9.8%
Bank Deposits	0	(279)	—	0	(279)	—
Building & Loan Association	0	0	—	71,384	36,375	96.2
Distilled Spirits	87,769	234,935	-62.6	87,769	264,670	-66.8
General - Intangible	20,294,490	21,550,380	-5.8	20,298,320	21,477,621	-5.5
General - Real	136,386,530	122,776,207	11.1	136,609,630	122,831,185	11.2
General - Tangible	65,085,999	61,055,235	6.6	86,807,551	76,958,174	12.8
Omitted & Delinquent	6,605,289	3,008,775	119.5	11,361,580	5,817,451	95.3
Public Service	24,564,927	15,762,469	55.8	36,335,053	38,003,455	-4.4
Other	4,667	51,283	-90.9	20,497	63,304	-67.6
Inheritance	\$12,513,315	\$17,417,289	-28.2%	\$31,672,876	\$36,566,560	-13.4%
Miscellaneous	\$8,136,246	\$8,783,054	-7.4%	\$17,097,216	\$17,964,923	-4.8%
Legal Process	5,947,534	6,603,950	-9.9	12,881,674	13,849,486	-7.0
T. V. A. In Lieu Payments	2,169,899	2,156,929	0.6	4,196,730	4,093,262	2.5
Other	18,813	22,175	—	18,813	22,175	-15.2
Nontax Receipts	\$99,695,567	\$85,360,274	16.8%	\$172,257,253	\$148,973,899	15.6%
Departmental Fees	5,092,736	5,170,194	-1.5	11,060,044	11,141,417	-0.7
PSC Assessment Fee	75,361	1,754	4197.5	11,108,369	5,446,193	104.0%
Fines & Forfeitures	6,262,042	7,733,579	-19.0	12,842,763	14,494,560	-11.4
Interest on Investments	199,013	351,311	-43.4	440,215	598,821	-26.5
Lottery	41,752,000	40,000,000	4.4	86,752,000	82,800,000	4.8
Sale of NOx Credits			—	3,340,425	5,364,325	
Miscellaneous	46,204,415	29,670,361	—	46,713,438	29,128,582	60.4
Redeposit of State Funds	\$1,260,372	\$1,737,959	-27.5%	\$2,603,339	\$6,886,742	-62.2%

KENTUCKY STATE GOVERNMENT REVENUE - ROAD FUND REVENUE

	Second Quarter 2004 - 2005	Second Quarter 2003 - 2004	% Change	Year-To-Date 2004 - 2005	Year-To-Date 2003 - 2004	% Change
TOTAL ROAD FUND	\$256,663,036	\$258,345,178	-0.7%	\$542,568,469	\$551,918,494	-1.7%
Tax Receipts-	\$249,531,336	\$251,812,298	-0.9%	\$527,833,716	\$531,996,155	-0.8%
Sales and Gross Receipts	\$208,570,222	\$211,973,554	-1.6%	\$445,088,069	\$447,445,775	-0.5%
Motor Fuels Taxes	112,616,058	108,681,999	3.6	234,486,374	220,850,733	6.2
Motor Fuels Use & Surtax	3,585,481	5,269,623	-32.0	8,586,467	9,897,977	-13.3
Truck Trip Permits (fuel)	103,415	106,600	-3.0	237,580	204,120	16.4
Motor Vehicle Usage	92,265,268	97,915,332	-5.8	201,777,648	216,492,946	-6.8
License and Privilege	\$40,961,113	\$39,838,744	2.8%	\$82,745,647	\$84,550,380	-2.1%
Motor Vehicles	14,512,307	15,422,496	-5.9	31,338,262	36,733,066	-14.7
Motor Vehicle Operators	1,399,627	1,392,199	0.5	3,031,645	2,809,168	7.9
Weight Distance	20,825,566	19,630,044	6.1	41,612,294	39,308,177	5.9
Truck Decal Fees	678,944	19,717	3343.4	810,472	52,511	1443.4
Other Special Fees	3,544,669	3,374,287	5.0	5,952,974	5,647,458	5.4
Nontax Receipts	\$6,899,806	\$6,036,427	14.3%	\$14,357,482	\$19,156,931	-25.1%
Departmental Fees	4,114,439	3,295,291	24.9	8,580,313	7,218,718	18.9
In Lieu of Traffic Fines	325,579	373,217	-12.8	694,884	766,803	-9.4
Highway Tolls	1,481,524	1,561,921	-5.1	3,113,743	4,772,210	-34.8
Investment Income	824,778	619,250	33.2	1,724,629	6,047,091	-71.5
Miscellaneous	153,486	186,748	-17.8	243,913	352,108	-30.7
Redeposit of State Funds	\$231,895	\$496,453	-53.3%	\$377,271	\$765,408	-50.7%

1 *Executive Summary*

3 *The Economy*

9 *Revenue Receipts*

11 *Economic and Revenue Outlook*

19 *Appendix: Second Quarter Receipts*
